

Message Text

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INFO OCT-01 ISO-00 AEC-05 AID-05 CEA-01 CIAE-00 CIEP-01

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TO SECSTATE WASHDC 7673

INFO AMEMBASSY DUBLIN

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C O N F I D E N T I A L SECTION 01 OF 03 LONDON 01290

DEPT PASS TREASURY

E.O. 11652: GDS

TAGS: ENRG

SUBJECT: PETROLEUM REVENUE TAX: PAYMASTER GENERAL DELL
STATEMENT ON INDUSTRY CONSULTATIONS

BEGIN UNCLASSIFIED

1. ON JANUARY 16 PAYMASTER GENERAL DELL MADE A STATEMENT TO HOUSE OF COMMONS COMMITTEE ON OIL TAXATION BILL IN WHICH HE REFERRED TO HMG'S INTENTION TO MAKE SUITABLE PROVISION FOR MARGINAL FIELDS AND TO ITS FURTHER CONSIDERATION OF RATE OF PETROLEUM REVENUE TAX (PRT) AND TREATMENT OF NATURAL GAS. HE ALSO DESCRIBED CERTAIN AMENDMENTS WHICH GOVERNMENT PROPOSES TO BILL IN LIGHT OF CONSULTATIONS WITH INDUSTRY.

2. DELL NOTED HMG INTENDS THAT PROVISION BE MADE FOR AFFORDING DISCRETIONARY AND NON-DISCRETIONARY ASSISTANCE
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TO DEVELOPMENT OF MARGINAL FIELDS. AS TO DISCRETIONARY METHOD, IT WILL BE PROPOSED, HOPEFULLY SIMPLY AS A FALL-

BACK, THAT SECSTATE FOR ENERGY SHOULD HAVE POWER, WITH CONSENT OF TREASURY, TO DEFER, WAIVE OR REFUND ROYALTIES IN WHOLE OR IN PART. WHILE SUCH REFUNDS WILL BE FREE OF PRT, WHETHER OR NOT THEY SHOULD BE FREE OF CORPORATION TAX AS WELL IS STILL BEING CONSIDERED. CRITERIA WILL BE SPECIFIED FOR GRANT OF SUCH ASSISTANCE.

3. WITH RESPECT TO NON-DISCRETIONARY METHOD OF ASSISTANCE FOR MARGINAL FIELDS, DELL SAID DECISION NOT YET TAKEN AS TO HOW PROVISION WILL BE MADE WITHIN STRUCTURE OF PRT. HE NOTED INDUSTRY HAS MADE NUMBER OF PROPOSALS AND LISTED MAIN ONES AS: (A) A LOWER PRT RATE FOR MARGINAL FIELDS, (B) PRT SHOULD BE A GRADUATED TAX, PERHAPS ON PROFIT PER BARREL, (C) THERE SHOULD BE INCREASED UPLIFT FOR EXPENDITURE, (D) THERE SHOULD BE EXEMPTION OF A FIXED AMOUNT OR PROPORTION OF RECEIPTS FROM A FIELD, (E) THERE SHOULD BE A GUARANTEED MINIMUM RETURN. DELL OBSERVED HMG IS NOW TESTING ALL THESE PROPOSALS AGAINST INFORMATION GIVEN BY COMPANIES AND WILL PUT FORWARD ITS OWN PROPOSALS ON REPORT.

4. ON PRT RATE, DELL SAID THIS IS MOST IMPORTANT DECISION TO BE TAKEN. HMG IS ANALYZING CONSIDERABLE AMOUNT OF INFORMATION SUPPLIED BY COMPANIES AND HOPED ANNOUNCEMENT MIGHT BE MADE BY END OF FEBRUARY OR SOONER IF POSSIBLE.

5. ON GAS, DELL STATED HMG HAD ALWAYS BEEN AWARE THAT BECAUSE OF CONDITIONS OF SALE, IT PRESENTED A SPECIAL PROBLEM. GOVERNMENT CALCULATIONS SEEMED TO SHOW THAT BILL'S PROVISIONS TAKING INTO ACCOUNT ONLY RECEIPTS AFTER NOVEMBER 1974 WOULD BRING ABOUT A SUBSTANTIAL DEFERMENT OF LIABILITY TO TAX ON EXISTING FIELDS, AND THAT IN SOME CASES THERE WOULD BE NO LIABILITY AT ALL. HOWEVER, INDUSTRY HAD ASKED THAT GAS SHOULD BE EXEMPT FROM PRT AND WHILE THAT WOULD GO BEYOND WHAT WAS INTENDED WHEN BILL WAS INTRODUCED, PROPOSAL IS UNDER CONSIDERATION. DELL ADDED THAT ANY PROVISIONS WHICH MIGHT BE MADE FOR

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MARGINAL FIELDS ALSO MIGHT BE OF ADDITIONAL ASSISTANCE
TO EXISTING GAS FIELDS.

6. DELL ALSO ANNOUNCED A NUMBER OF AMENDMENTS ON VARIOUS
ASPECTS OF OIL TAXATION BILL WHICH HMG HAD TABLED RELATING
TO VALUATION OF OIL, VALUATION OF STOCK, SEPARATE CLAIMS
FOR EXPENDITURES BY LICENSES, OPTION TO SPREAD CAPITAL
EXPENDITURE, EXTENSION OF LIMIT FOR EXPLORATION EXPENDI-
TURE, EXPENDITURE RELATED TO CLOSING DOWN OF A FIELD AND
RELAXATION IN RULES FOR ABORTIVE EXPLORATION EXPENDITURE.
DELL SAID HE HAD AGREED IN PRINCIPLE BUT NOT TABLED DETAI
AMENDMENTS RELATING TO EXPENDITURE ON ASSETS AFTER AC-
QUISITION, INITIAL TREATMENT AND STORAGE, UNRELIEVED LOSS
ON A FIELD AND SELLING COSTS FOR CRUDE OIL.

7. COPIES OF DELL STATEMENT ARE BEING POUCHED TO EB/ORF/
FSE AND TREASURY. END UNCLASSIFIED
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8. COMMENT: INDUSTRY OFFICIALS FIND DELL'S STATEMENT
ONLY MILDLY ENCOURAGING. THEY NOTE DELL AND OTHER HMG
OFFICIALS HAVE MADE REASSURING PRONOUNCEMENTS BEFORE, AND

THEN COMPLETELY IGNORED INDUSTRY VIEWS IN TAKING DECISION ON MAJOR OFFSHORE POLICY ISSUES. NONETHELESS, IN A PERIOD WHEN SKYROCKETING DEVELOPMENT COSTS AND UNCERTAINTY OVER LIKELY DIRECTION OF GOVERNMENT POLICY HAVE BEGUN TO ADVERSELY AFFECT INVESTMENT CLIMATE, LATEST INDICATION THAT HMG IS STILL WILLING TO CONSIDER CHANGES IN PRT IS WELCOME SIGN. SENIOR HMG OFFICIALS NOW CONCEDE AT LEAST THAT DEVELOPMENT COSTS HAVE BEEN UNDERESTIMATED, THAT EVEN MODERATE SIZE FIELDS COULD BECOME "MARGINAL" UNDER PRESENT PROPOSALS AND THAT REVISED TAX FRAMEWORK MUST ENSURE THEY DO NOT PROVE UNECONOMIC TO DEVELOP.

9. OIL TAXATION BILL IS SCHEDULED TO LEAVE COMMITTEE ON FEBRUARY 4 OR 5. WITHIN TWO WEEKS THEREAFTER, GOVERNMENT SHOULD MAKE KNOWN ON REPORT EXACT NATURE OF PROPOSED AMENDMENTS EMBRACING MARGINAL FIELDS, PRT RATE AND TREATMENT OF GAS. UNLESS REASONABLY FORTHCOMING, CONSERVATIVE OPPOSITION IN PARLIAMENT WITH INDUSTRY SUPPORT IS LIKELY TO STAGE FULL-SCALE, BITTER POLITICAL DEBATE.

10. IN RECENT WEEKS INDUSTRY AT LEAST TEMPORARILY HAS HEALED SPLIT BETWEEN LARGEST COMPANIES POSSESSING PREPONDERANCE OF NORTH SEA RESERVES LOCATED IN BIGGEST FIELDS AND REST OF COMPANIES WHO ARE LESS WELL-ENDOWED. UNTIL RECENTLY SMALLER COMPANIES FELT BP, SHELL AND EXXON HAD ADVOCATED FIXED PRT RATE TO DETRIMENT OF MARGINAL FIELDS AND STOOD ALOOF OF UK OFFSHORE OPERATORS ASSOCIATION (UKOOA) EFFORTS ON PRT BECAUSE THEIR FORTIES AND BRENT FIELDS WERE ONLY ONES (BESIDES PIPER GROUP LED BY OCCIDENTAL) WHICH ALLEGEDLY COULD AFFORD IMPOSITION OF HIGH PRT RATE. BIG THREE WERE ACCUSED BY SOME SMALLER COMPANIES OF NOT WANTING TO TARNISH THEIR OWN IMAGE WITH HMG BY FIGHTING PRT TOO HARD OR, LESS CHARITABLY, OF WANTING TO PICK UP THE PIECES ONCE REST OF COMPANIES GAVE UP ON NORTH SEA DEVELOPMENT. THIS LAST ACCUSATION WAS MADE WITH PARTICULAR FORCE AGAINST BP AND, TO A LESSER
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EXTENT AGAINST SHELL (WITH EXXON AS NON-OPERATING PARTNER OF SHELL GOING ALONG FOR THE RIDE, GIVING QUIET SUPPORT TO BP/SHELL POSITION). IN INTEREST OF INDUSTRY SOLIDARITY BP, SHELL AND EXXON DID JOIN IN LAST SUBMISSION MADE BY

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UKOOA TO DELL WHICH EMPHASIZED SITUATION IS SERIOUS AND COMPANIES ARE NOT BLUFFING ABOUT CONSEQUENCES FOR NORTH SEA DEVELOPMENT IF HMG PROCEEDS AS PLANNED.

11. FROM FINANCIAL STANDPOINT, AT LEAST ONE BANK HAS MADE CLEAR TO HMG IT DOES NOT WANT TO LEND ON BASIS OF A PRT THAT WILL CHANGE FOR A GIVEN FIELD. BANK WANTS SECURITY AND THIS MEANS ANY FLEXIBILITY IN PRT SHOULD BE BUILT INTO SPECIFIC RATES APPLIED BASED ON SIZE AND COST OF INDIVIDUAL FIELDS.

12. IT IS STILL AN OPEN QUESTION WHETHER HMG WILL ACCEPT SOME INDUSTRY ESTIMATES THAT FIELDS OF LESS THAN 300 MILLION BARRELS OF RESERVES PER PRODUCTION PLATFORM CANNOT AFFORD ANY PRT AT ALL. LABOR GOVERNMENT SUSPICION THAT OIL COMPANIES ARE SEEKING TO AVOID TAXATION RUNS DEEP. COMPANIES WERE, IN FACT, UNDULY OPTIMISTIC IN EARLY 1970'S
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ABOUT NORTH SEA POTENTIAL IN ORDER TO IMPRESS FINANCIAL INSTITUTIONS AND OBTAIN REQUIRED LOANS. WHILE BANKERS

HAVE RECENTLY SHIED AWAY AS RESULT OF ESCALATING COSTS, UNCERTAIN GOVERNMENT POLICY AND POORER GEOLOGICAL PROSPECTS, HMG IS PERHAPS JUST BEGINNING TO ACCEPT WHAT INDUSTRY AND BANKERS NOW CONSIDER TO BE REALISTIC APPRAISAL OF NORTH SEA DEVELOPMENT COSTS AND PROFIT AND TAXATION POTENTIAL. SUBSTANTIAL GAP BETWEEN CONFLICTING POINTS OF VIEW IS NARROWING BUT A GAP NONETHELESS STILL REMAINS.

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